No. 86-904

In the Supreme Court of the United States

OCTOBER TERM, 1986

ROBERT B. TRAINER AND SIRIN D. TRAINER, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FEDERAL CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

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Petitioners contend that the "add-on minimum tax" formerly imposed by 26 U.S.C. (1976 ed.) 56 was an excise tax, which may be deductible against gross income under some circumstances, rather than an income tax, which is not deductible. This contention has been correctly and uniformly rejected by every court that has considered it, and it does not warrant further review.

1. Petitioners brought this suit in the United States Claims Court for refund of income taxes for 1974 and 1976-1980. During the relevant tax years, Section 56 of the Internal Revnue Code, as then in effect, imposed a "minimum tax on tax preferences" that was payable in certain circumstances by both individual and corporate taxpayers. Section 56(a) provided in 1976 that "[i]n addition to the other taxes imposed by this chapter, there is hereby imposed for each taxable year, with respect to the income of

every person, a tax equal to 15 percent of the amount by which the sum of the items of tax preference exceeds" a specified base amount. This provision was generally referred to as the "add-on minimum tax."[1]

On their tax returns for 1976-1980, petitioners took the position that the minimum tax formerly imposed by Section 56 was an excise tax and hence that it was deductible in computing their taxable income either as an ordinary and necessary business expense (I.R.C. § 162) or as an expense for the production of income (I.R.C. § 212).[2] The Commissioner disallowed the deductions on the ground that the tax imposed by Section 56 was a federal income tax; Section 275(a)(1) of the Code expressly provides that "[n]o deduction shall be allowed for * * * Federal income taxes." As a result of the disallowance of petitioner's claimed minimum-tax deductions for 1977, the amount of investment tax credit available for a carryback to 1974 was also reduced.

After paying the resulting tax deficiencies and filing unsuccessful claims for refund, petitioners brought this refund suit in the Claims Court. Relying on its prior holding in *Mobley* v. *United States*, 8 Cl. Ct. 767 (1985), the Claims Court sustained the Commissioner's position (Pet. App.

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[1]The add-on minimum tax at issue here was repealed in 1982. Tax Equity and Fiscal Responsibility Act of 1982, Pub. L. No. 97-248, § 201(d), 96 Stat. 419. During 1983-1986, Section 55 of the Code set forth an "alternative minimum tax" payable by taxpayers other than corporations, and Section 56 set forth a "corporate minimum tax." Compare 26 U.S.C. 55 and 56 with 26 U.S.C. (1976 ed.) 56. Those two provisions in turn were repealed by the Tax Reform Act of 1986, Pub. L. No. 99-514, § 701, 100 Stat. 2320, which created a new "alternative minimum tax" payable by both individuals and corporations. The current version of the minimum tax bears little resemblance to the 1976 version that is at issue here.

[2]Unless otherwise noted, all statutory references are to the Internal Revenue Code (26 U.S.C.), as amended (the Code or I.R.C.).

22a-26a). In *Mobley*, the taxpayers had contended that the imposition of the minimum tax on intangible drilling costs and excess depletion deductions constituted taxation upon the recovery of capital, not upon net income, and hence that the minimum tax was an excise tax. The Claims Court in *Mobley* stated: "Faced with the plain language of the statute, its legislative history, and the holdings of [this and] other courts, we hold that the minimum tax is an income tax." 8 Cl. Ct. at 771. Citing that holding, the Claims Court in the instant case granted the government's motion for judgment on the pleadings and dismissed petitioners' complaint. The court of appeals unanimously affirmed (Pet. App. 13a, 21a).

2. Petitioners contend (Pet. 4-21) that the minimum tax formerly imposed by 26 U.S.C. (1976 ed.) 56 was not an income tax and hence that they were entitled to take a deduction for their minimum tax payments. The gist of their contention is that some of the items of tax preference listed in 26 U.S.C. (1976 ed.) 57, which formed the predicate for the computation of the Section 56 tax, were not items of income, but instead were items of capital recovery, such as accelerated depreciation and depletion allowances. See Pet. App. 3a-6a. Petitioners assert that the minimum tax was "imposed on the privilege of utilizing certain provisions under the Code for the purpose of computing the income tax" (Pet. 4), and hence that the tax was not itself an income tax but rather was an excise tax.

Petitioners acknowledge (Pet. 4, 6) that the statutory language and congressional intent are squarely contrary to their position. Section 56 was contained in Subtitle A, Chapter 1, Subchapter A of the Internal Revenue Code. Subtitle A is entitled "Income Taxes"; Chapter 1 is entitled "Normal taxes and surtaxes"; and Subchapter A is entitled "Determination of tax liability." Section 56 itself provided that the tax it prescribed was "imposed * * * *with respect to*

the income" of the taxpayer (26 U.S.C. (1976 ed.) 56(a) (emphasis added)). See also 26 C.F.R. 1.56-1 (1979).

The legislative history confirms Congress's intent that the minimum tax be imposed on the taxpayer's income. Congress enacted the minimum tax, "in addition to the regular income tax," upon "tax preference income in excess of the specified exemption" (S. Rep. 91-552, 91st Cong., 1st Sess. 113 (1969)). Congress intended thereby to increase the income tax liability of persons whose regular income tax liability was disproportionately reduced by claiming excessive exclusions, credits, and deductions, many of which (like accelerated depreciation and depletion) did not reduce the taxpayer's current income in an economic sense. *Wyly* v. *United States*, 662 F.2d 397, 405 (5th Cir. 1981); see also *Ward* v. *United States*, 695 F.2d 1351, 1355 (10th Cir. 1982). The minimum tax was thus designed by Congress to "reduce drastically the ability of individuals to escape payment of tax on economic income" (H.R. Rep. 91-413, 91st Cong., 1st Sess. Pt. 1, at 78 (1969)). See also *Lubus* v. *United States*, 78-1 U.S. Tax Cas. (CCH) ¶ 9242 (2d Cir. 1978) ("Congress's intention was * * * to impose an additional tax on high income individuals with large amounts of nonwage income.").[3] Thus, as the court of appeals noted (Pet. App. 17a), permitting such taxpayers to deduct their minimum tax payments by characterizing them as excise taxes "would obviously frustrate the intent of Congress."[4]

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[3]This position was reaffirmed by the 99th Congress when it stated that the minimum tax serves one overriding objective: "[T]o insure that no taxpayer with substantial *economic income* can avoid significant tax liability by using exclusions, deductions, and credits." S. Rep. 99-313, 99th Cong., 2d Sess. 518 (1986) (emphasis added).

[4]The court of appeals correctly rejected (Pet. App. 20a n.7) petitioners' invocation (Pet. 7-9) of Treas. Reg. § 1.901-2 and Rev. Rul. 78-61, 1978-1 C.B. 221, which are addressed to the issue of whether a foreign tax should be regarded as an "income tax" for purposes of the foreign tax credit. The criteria used to evaluate foreign taxes have no direct

Petitioners' argument thus boils down to the assertion that, "notwithstanding statutory language or congressional intent to the contrary" (Pet. 6), the minimum tax must *necessarily* be an excise tax, since, if it were an income tax, it would be unconstitutional. The Sixteenth Amendment, as petitioners note, empowers Congress to lay a tax upon "incomes" without apportionment among the states. Petitioners contend that the Section 56 tax was not laid upon "incomes" in the constitutional sense because it was computed by partial reference to certain deductions that reflect recovery of capital. From this premise, petitioners reason that the tax formerly imposed by Section 56 could pass constitutional muster only if it were styled an "excise tax."

The premise of petitioners' argument is plainly incorrect. The fact that the Section 56 tax was computed by reference to specified items of tax preference does not mean that the tax was an excise tax *on* those items, which generally speaking are deductions allowed elsewhere in the Code. Rather, as the court of appeals explained (Pet. App. 19a), the Section 56 tax, "[a]s a matter of substance," merely reduced the economic value of those preferential deductions by restricting the taxpayer's ability to use them to offset other income on his tax return. Thus, while "the total of tax preferences serves as the tax base" for computational purposes (Pet. App. 19a), the effect of the minimum tax is just a reduction in the otherwise-allowable tax deductions, yielding a higher total tax on the taxpayer's *income*. The tax is actually imposed upon an amount of income equal to the preferential deductions and exclusions that are effectively disallowed; the tax is not imposed on the preferences themselves (*id.* at 18a n.6).

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application here where Congress has plainly established the minimum tax as an income tax; moreover, Rev. Rul. 78-61 expressly recognizes that the United States income tax sometimes taxes "the constructive or deemed receipt of income," which is what the court of appeals here (Pet. App. 20a n.7) found to be the substantive effect of the minimum tax. See also *Mobley* v. *United States*, 8 Cl. Ct. at 770.

For these reasons, every court that has considered the question has rejected the claim that the minimum tax is an excise tax. *Wyly* v. *United States, supra*; *Ward* v. *United States, supra; Lubus* v. *United States, supra*; *Kolom* v. *Commissioner*, 71 T.C. 235, 250 (1978), aff'd, 644 F.2d 1282 (9th Cir. 1981). In the words of the Fifth Circuit, "the minimum tax is imposed upon an individual's income, and the fact that it may be more closely tied to 'economic,' rather than taxable, income does not serve to change this result." *Wyly* v. *United States*, 662 F.2d at 405. And, although this Court has never been directly presented with the question of the proper characterization of the minimum tax as an income tax or as an excise tax, the Court has repeatedly referred to it as an "income tax." *United States* v. *Darusmont*, 449 U.S. 292, 294, 299 (1981); see Pet. App. 20a. Accordingly, petitioners' contention is erroneous and does not warrant review by this Court.[5]

It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

CHARLES FRIED
Solicitor General

FEBRUARY 1987

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[5]As noted above (note 1, *supra*), the "add-on minimum tax" at issue here has been repealed by Congress. The "alternative minimum tax" currently imposed by the Code is calculated quite differently from the old Section 56 tax, and, as petitioners acknowledge (see Pet. 18), the new "alternative minimum tax" is even more obviously an income tax than the provision involved here. Accordingly, even if the issue presented here were otherwise worthy of this Court's attention, this legislative change severely limits the impact of any decision that the Court would render in this case and makes it quite clear that review by this Court is not appropriate.